Macro | FX Research and Strategy

Global

FX Insight

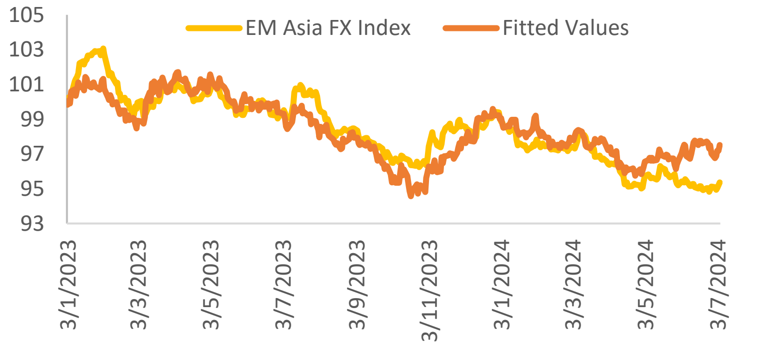
Is EM Asia FX Under Risk of Further Weakness?

Still Expect More Near Term EM Asia FX Weakness, Medium Term Strength

Over the last two years, EM Asia FX generally has been on a weakening trend that was driven by a variety of factors. This include 1) higher for longer rates environment; 2) EM assets looking less attractive; 3) EM risk off and political uncertainty; 4) deteriorating fundamentals; and 5) China economic weakness. These factors combined with other risk factors such as the upcoming US presidential elections with concerns about its impact on US trade policies and a still somewhat cautious Fed can result in the EM Asia FX currencies seeing more weakness in the upcoming months. However, we believe that the near future could mark the peak of weakness and subdued sentiment and that this would eventually turn especially as we come closer to the year end.

We have seen some improvement in risk sentiment recently with the more benign slowdown in US growth and gradual US disinflation, leading to an easing in USD and friendly for risk. Closer to year end and going into next year, risk-sentiment in the region we believe should improve. More importantly, aside from US related factors, domestic factors could play a part in ensuring the extent of the resilience of the EM currency. Concerns related to the US Presidential elections should dissipate whilst the Fed would engage in easing in a more certain manner. However, USD - Asia pairs may still trade at an elevated level into next year as UST yields may still trade at relatively high levels relative to domestic EM yields (even as they come down) due to a slow Fed pace of easing, inflationary risks of the next US administration and fiscal concerns of the US government. Overall, we are still positive on EM Asia FX but still stay somewhat cautious.

UST 10Y Yields Movements Explains Most of EM Asia FX Despite Deviations Recently



Source: Bloomberg, Maybank FX Research & Strategy
Note: Fitted values are derived from a least square regression of daily data with EM Asia FX index on UST 10Y yields between 1 Jan 2023 to 7 Jul 2024. EM Asia FX index is an equal weighted index of MYRUSD, IDRUSD, PHPUSD, THBUSD, SGDUSD, KRWUSD, INRUSD, VNDUSD and TWDUSD.

Analysts

Saktiandi Supaat
(65) 6320 1379
saktiandi@maybank.com

Alan Lau, CFA
(65) 6320 1378
alanlau@maybank.com

Fiona Lim
(65) 6320 1374
fionalim@maybank.com

Shaun Lim
(65) 6320 1371
shaunlim@maybank.com

Is EM Asia FX Under Risk of Further Weakness?

In recent times, regional Asia FX have generally come under pressure amid both idiosyncratic and external factors. Externally, higher for longer US rates has weighed on sentiment for the EM sentiment as the Fed has dialed on the number of cuts that it expects this year. However, anxiety has not stopped there as idiosyncratic factors have also hurt a number of these currencies. In this piece, we look to explore whether EM Asia FX would face further stress or if this period actually marks a buy for these currencies. We do note there has recently been strengthening in the EM Asia FX space although they have not fully recovered all their losses.

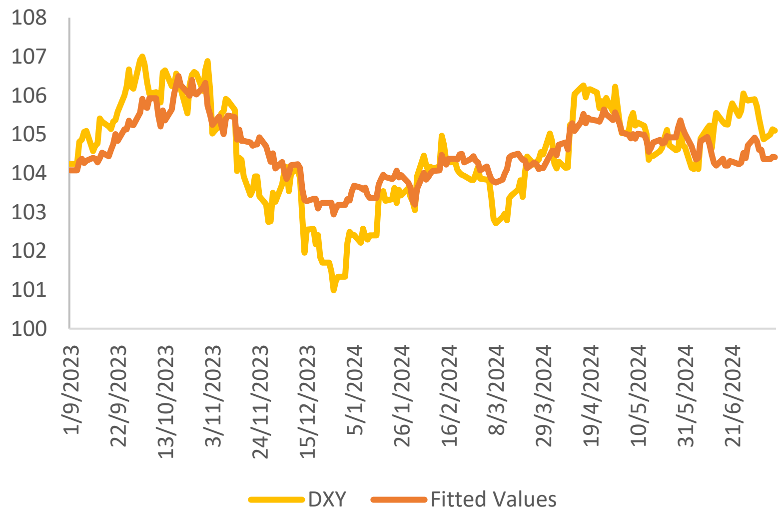
What are the Key Factors Driving EM Asia FX Weakness?

Over the last few months, there are a number of factors that have driven the weakness in Asia FX, with some less favorable developments. Some of these have both been external and global in nature whilst a number of them have also been idiosyncratic. These negative factors though happen to have coincidently come together at the same time and in combination badly hurt the Asia FX space. At this point, we ask the question whether many of these factors can persist.

1. The Higher for Longer Story in Rates

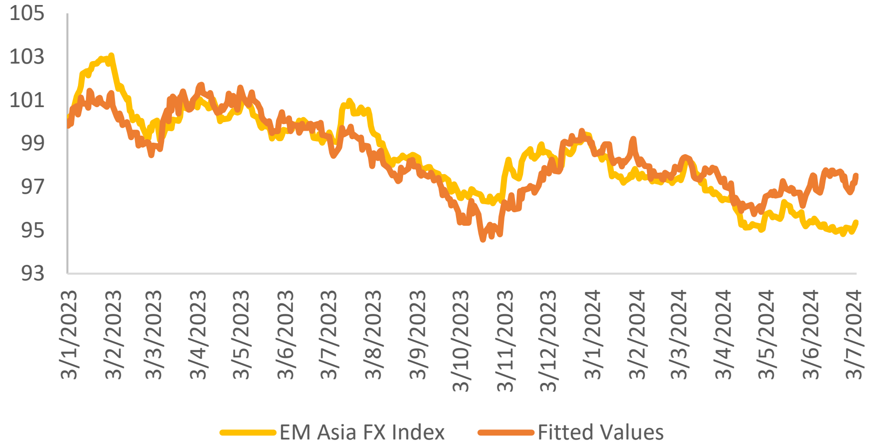
The Fed's rate path has been an ever changing narrative as we have constantly in the last few years swung between hopes of a cut only to see the Fed raise rates again or hold for much longer than we expect. Earlier this year, the dot plots had pointed to three rate cuts in 2024 although the latest updated plots now imply about one cut in 2024. At this point, markets see the possibility of about two - three cuts by end this year. The Fed has continued to stay adamant that an easing cycle is intact except that it has been delayed in some sense. Asia FX weakness undeniably has been driven by the Fed's higher for longer stance. High rates and UST yields is an elephant in the room, weighing on EM currencies. In the medium to long term, DXY strength is still driven by the UST 10y yields even if the sensitivity can deviate in the short run. USD – Asia pair also exhibit that relationship (with the exception of USDSGD).

Chart 1: DXY Exhibit a Strong Relationship with UST 10Y Yields



Source: Bloomberg, Maybank FX Research & Strategy
Note: Fitted values are derived from a least square regression of daily data with DXY on UST 10Y yields between 1 Jan 2023 to 7 Jul 2024

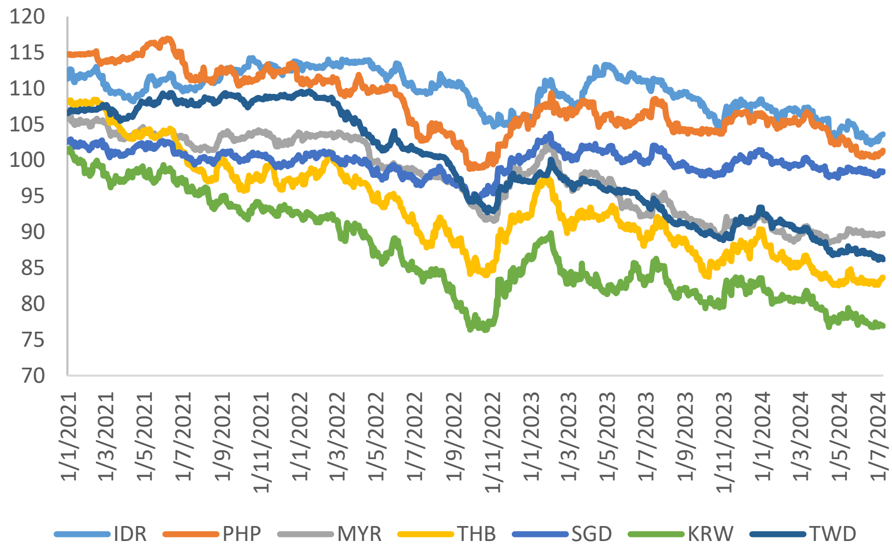
Chart 2: UST 10Y Yields Movements Explains Most of EM Asia FX Despite Deviations Recently



Source: Bloomberg, Maybank FX Research & Strategy
Note: Fitted values are derived from a least square regression of daily data with EM Asia FX index on UST 10Y yields between 1 Jan 2023 to 7 Jul 2024. EM Asia FX index is an equal weighted index of MYRUSD, IDRUSD, PHPUSD, THBUSD, SGDUSD, KRWUSD, INRUSD, VNDUSD and TWDUSD.

From a carry perspective, we have also noticed that returns have been on a decline for most EM Asia FX over the last year or so, which would also be in line with the climb in UST yields and USD – Asia pairs.

Chart 3: Carry Returns for EM Asia FX, Funded with USD Have been on a Decline Over the Years, Weighing on the Respective Currencies



Source: Bloomberg, Maybank FX Research & Strategy
Note: Carry is reflected as a result indexed to 1 Jan 1999 i.e. a reading of 100 implies that carry is identical to carry on 1 Jan 1999 and 200 implies a carry of 2 times carry on 1 Jan 1999. Computed based on borrowing JPY placing it in at the xxx three month deposit, and selling IDR in three months based on the forward rates on the day to unwind.

Table 1: Current High US Rates Implies that Even Two Fed Rate Cuts of 25bps this Year May Mean Differentials Can Remain Unfavorable

Country	2Y Yields (%)	10Y Yields (%)	Policy Rate Differential with the US (Country Rate - US Rate) (bps)	Expected Policy Rate Differential by end 2024
US	4.45	4.18	-	-
Eurozone	2.82	2.49	-125bps	-125bps
UK	4.07	4.11	-25bps	-50bps
Indonesia	6.67	6.93	75bps	125bps
Malaysia	3.48 (3Y)	3.84	-250bps	-200bps
Philippines	-	6.82	100bps	100bps
Thailand	2.32	2.61	-300bps	-250bps
South Korea	3.23	3.18	-200bps	-150bps
India	6.93	6.97	100bps	150bps

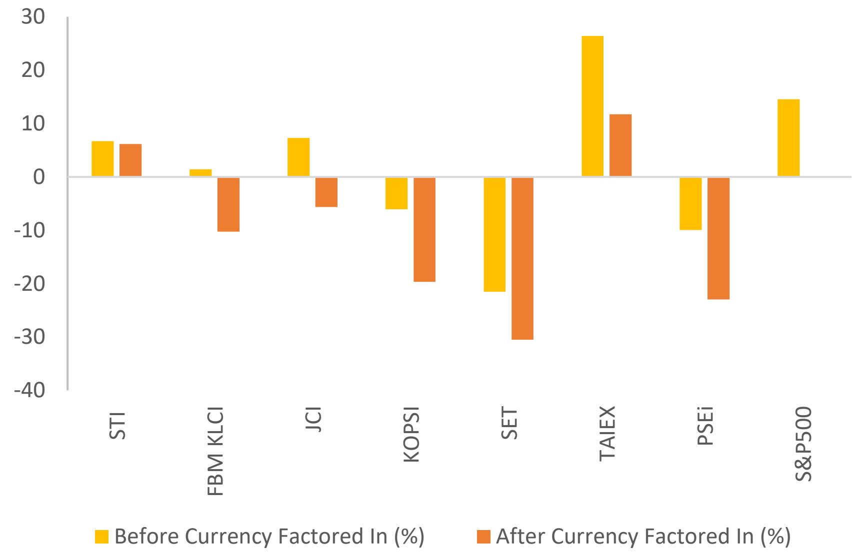
Note: 1. Yields and rates are as of 12 Jul 2024, 2. Expected policy rate differential is calculated based on where we forecast the individual central banks rate to be at by end 2024
Source: Bloomberg, Maybank FX Research & Strategy

2. EM Assets Look Less Attractive for Most

Meanwhile, we are also cognizant that Asia FX weakness at the same time has also made equity investments less attractive. Returns since 2022 for most Asia equity markets has been poorer than the S&P500 and currency losses only amplify the weakness. Despite the poor returns for some of these markets over the last couple of years, we somehow notice that equity inflows has been strong for some of these places such as Korea and Taiwan this year. This inflow could possibly be driven by the greater optimism for AI and chips stocks and indicates some turning for them in the equity space this year.

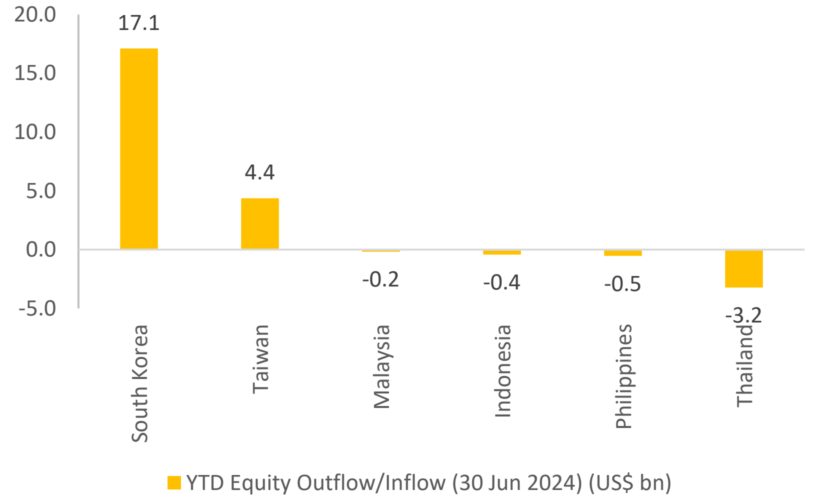
Meanwhile, in the bond space, we tend notice that it is more mixed within EM Asia. The more political pressured countries such as Thailand and Indonesia (elaborated more below) seem to be seeing substantial outflows year to date. For countries such as Malaysia, the inflow year to date is still tepid given that investors may still uneasy to position too strongly yet into their bonds amid a relatively hawkish leaning Fed still and given the country's low rates (reduced likelihood of cuts so soon). India has been seeing strong inflows due to inclusion into global indices but the central bank at the same time tries to ensure currency stability and prevents too much strengthening from this factor. As for South Korea, the positive benefits from strong inflows (also due to anticipation from inclusion into the global indicies) could be offset by the hedging against currency weakness.

Chart 4: Equity Returns in Asia Since 2022 Have Paled in Comparison to S&P500



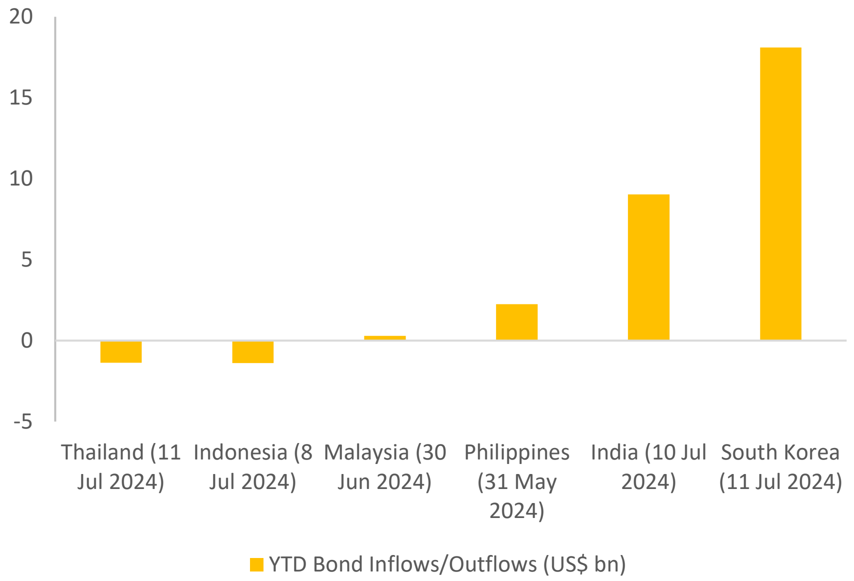
Source: Bloomberg, Maybank FX Research & Strategy

Chart 5: Equity Inflows this Year have Been Strong into Places such as South Korea and Taiwan and that Could Signal a Turnaround Allowing Equities to be a Supportive Element for some EM Asia FX



Source: Bloomberg, Maybank FX Research & Strategy

Chart 6: Bond Inflows Performance is Mixed Within EM Asia



Source: Bloomberg, Maybank FX Research & Strategy

3. EM Risk Off and Political Uncertainty

Beyond a rates perspective, we are also cognizant that political uncertainty within the EM space is also not helping. No doubt that this has weighed on the EM FX space heavily. However, we are not anticipating that the situation can get worse from here. If anything, we do see that this concern has passed already especially with the recovery in the MXN and ZAR whilst the INR has stabilized. Carry returns for many of EM currencies are still favorable, especially if funded with the JPY and therefore, appetite for EM currencies are likely to still hold up in the medium term from this angle.

We do note there are some currencies within the EM space that can still risk being further weighed down by their own recent idiosyncratic political uncertainties too. This includes Thailand where we sense markets have mainly priced in the political situation as it is, where the government remains in power but political bickering persists. With the CDS prices having fallen much lower from their highs of the election last year, we believe that markets have not yet factored a further deterioration of the political situation. We stay cognizant of this given the current court cases that Prime Minister Srettha and former Prime Minister Thaksin Shinawatra face. Into end 2025, within regional EM Asia, there are two major elections, which are the Philippines Mid-Term General Elections (Senate and House of Representatives) on 12 May 2025 and Singapore General Elections that have to be held by 23 Nov 2025.

Table 2: Key Asia Elections Until End 2030

Date	Country	Election
12 May 2025	Philippines	Mid-Term General Elections (Senate and House of Representatives)
By 23 Nov 2025	Singapore	General Elections - Parliament
2026	Vietnam	Legislative Election
3 Mar 2027	South Korea	Presidential Election
By 27 Jun 2027	Thailand	General Election - House of Representatives
Apr 2028	South Korea	Legislative Election
By 17 Feb 2028	Malaysia	General Election
2028	Philippines	Presidential and General Election (Senate and House of Representatives)
2029	Indonesia	General Election - Presidential and Legislative
2030	Singapore	General Elections - Parliament

Source: Various Online Sources, Maybank FX Research & Strategy

Table 3: Political Business Cycle Risks and Currency Impact

Region	Country	Average PBC Length	Length of Electoral Cycle	General correlation to currency
US		3	4	Yes
UK		4	2-5*	Yes
Asia	Singapore	5	5	Only after 2017
	Malaysia	4	5	No
	Thailand	6	2-5*	No
	Philippines	4	3*	Yes
	Indonesia	4	5	Yes, except 2010-2018

Source: Maybank FX Research & Strategy

4. Deteriorating Fundamentals

We note that idiosyncratically, quite a number of EM Asia countries have either seen or are facing the risk of deteriorating fundamentals. In particular, both Thailand and Indonesia face potential fiscal concerns amid the ambitious economic plans of newly elected political leaders.

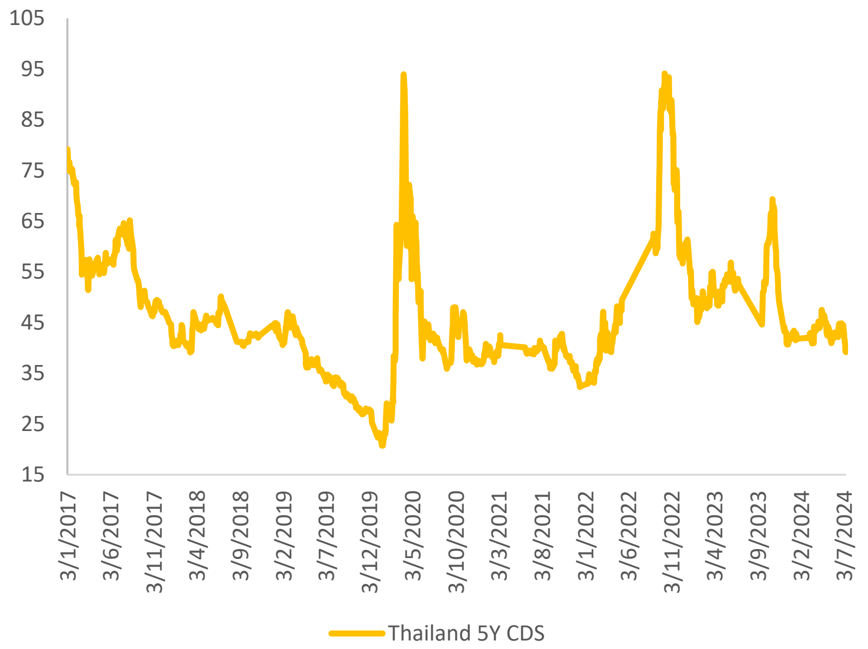
Indonesia's President – Elect Prabowo aims to boost Indonesia's economic growth in addition to improving the social conditions of their citizens. Our own economist has written a piece that looks into Prabowo's plans and the initiatives he would undertake. The main concerns around his plans at this point is the level of which he would raise the debt-to-GDP ratio and the fiscal deficit. Regarding the former, Bloomberg has reported that it could be increased to 50.0% from the current 39.0% whilst there are talks that the President – elect could raise legal limit for the fiscal deficit of 3%. Currently though, there has already been plenty of concerns about his fiscal plan that has been expressed in the market. However, the question is how much of this concern has already been priced in. We acknowledge there is no perfect way to measure the level to which political concerns have been priced in but examining the CDS prices can give some idea. If we look at the 5Y CDS for Indonesia, it has nearly hit levels close to April when Prabowo was confirmed the winner and above that seen early in the year when the election was ongoing. Despite being at around levels close to points when there was higher political uncertainty this year, we cannot rule out further climbs in the CDS. The reason behind this is that if we look at the CDS over the years, we see that the CDS price has tended to trend lower overtime throughout Jokowi's term. This could be some reflection of the improvement in fiscal discipline during his time as President. Under a new Prabowo government, the risk stands as discussed for this to reverse. Therefore, we stay cautious about the impact of fiscal and political factors on the IDR.

Chart 7: A Decline in the Indonesia 5Y CDS is Partly a Reflection of Improved Credibility in Indonesia's Fiscal Management (and also the Improved Global Risk Environment)

Source: Bloomberg, Maybank FX Research & Strategy

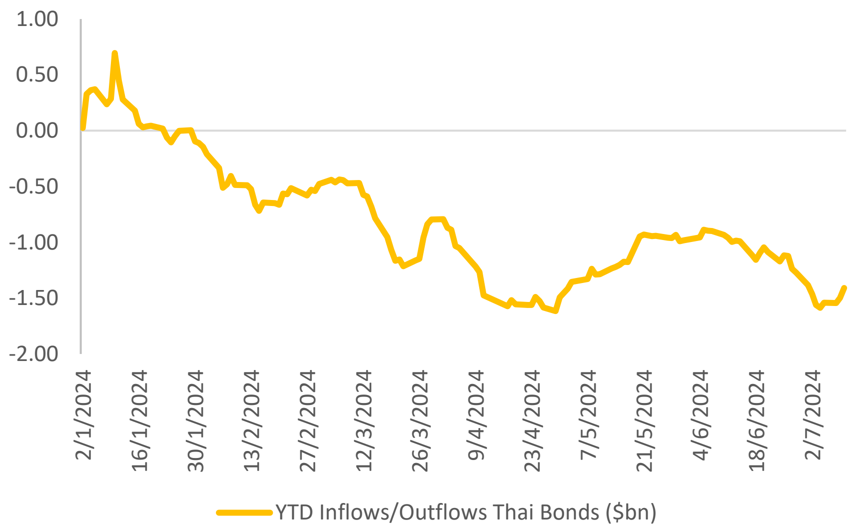
Meanwhile, Thailand's PM Srettha is attempting to strongly reinvigorate the economy, which involves among other measures the rollout of the digital wallet handout. There is still quite some uncertainty about whether this measure and even Srettha's latest budget can pass and also be implemented successfully. If we look at the Thai 5Y CDS, we find that after trending lower in the pre-pandemic period, it is trading at somewhathigher level, which could be reflective of more political and fiscal concerns. If we look at the monthly bond flow data for Thailand, there was an outflow in Jun but there was a strong inflow in May. On year to date basis, outflow has been high at -$1.4bn (as of 10 Jul 2024), which puts it among the worse within the Asia region. Putting all this information together, we do not think the THB can be further weighed down by the current political situation as the market has likely already priced it in. However, if the political situation does significantly deteriorate from where we are right now, then the THB can see further weakness.

Chart 8: After Trending Downwards Pre-Pandemic, Thailand 5Y CDS is Trading Somewhat Higher, Possibly Reflecting More Political and Fiscal Concerns



Source: Bloomberg, Maybank FX Research & Strategy

Chart 9: Year to Date Outflows for Thai Bonds has Been High Which in Some Sense Reflects Concerns about the Country Domestic and Economic Situation



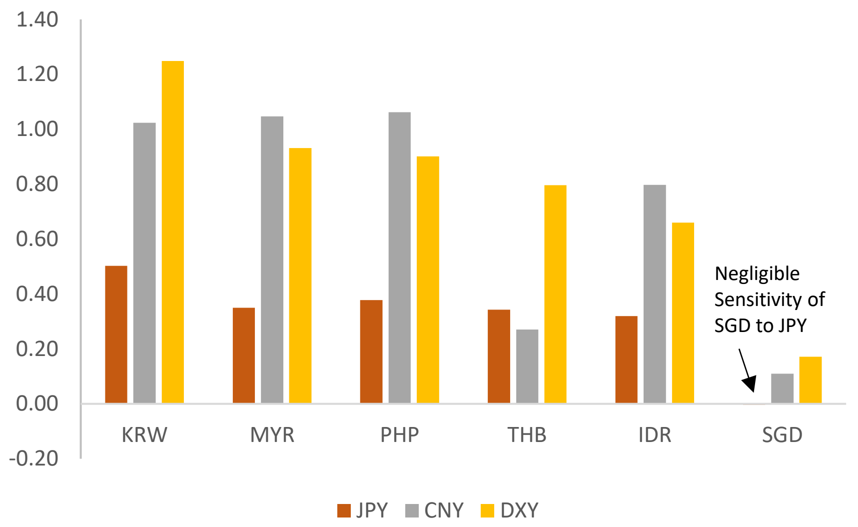
Source: Bloomberg, Maybank FX Research & Strategy

5. China Economic Weakness

Based on our analysis, we have found that USD – Asia pairs has exhibited greater level of sensitivity to the USDCNY. This is not surprising given the strong trade links between China and the regional Asia EMs. The USDCNY over the last 2 – 3 years have gradually edged up overtime amid concerns about the state of the Chinese economy and so have the USD – Asia pairs. However, we do notice that this relationship has somewhat not quite been as strong in recent times. Regardless, on a medium to long term period, it likely still holds given the trade links. Therefore, if the Chinese economy does turn around and the CNH gets a lift, then other EM Asia FXs could also get supported.

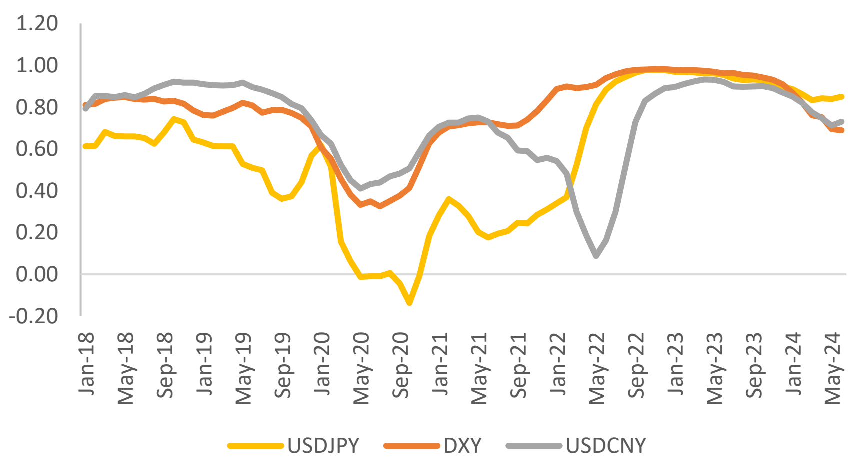
As a side note, we would like to mention that the JPY did see quite some strengthening in recent times. Our analysis has shown that a number of EM Asia FX can have quite some sensitivity to the JPY. In some sense, this did kind of play out as the USD – Asia pairs did generally come down quite strongly on the same day that the USDJPY had sharply fallen. Our current forecast though does see the USDJPY rebounding into the third quarter as yield differentials are likely to stay unfavorable and any current JPY strength is only temporary. Therefore, in line with the JPY, Asia FX can risk weakening further again after this bout of strength.

Chart 10: A Number of the EM Asia FX Exhibit Strong Sensitivity to the CNY and therefore, China Weakness Can Weigh Substantially on Them



Source: Bloomberg, Maybank FX Research & Strategy
Note: Sensitivity is calculated based on weekly data for the period of Jan 2015 - Jun 2024 and the Y axis is beta sensitivity

Chart 11: We Do Note that the USDCNY Correlation with EM Asia FX is Lower Recently But The Relationship Between the Two Historically has Been Strong



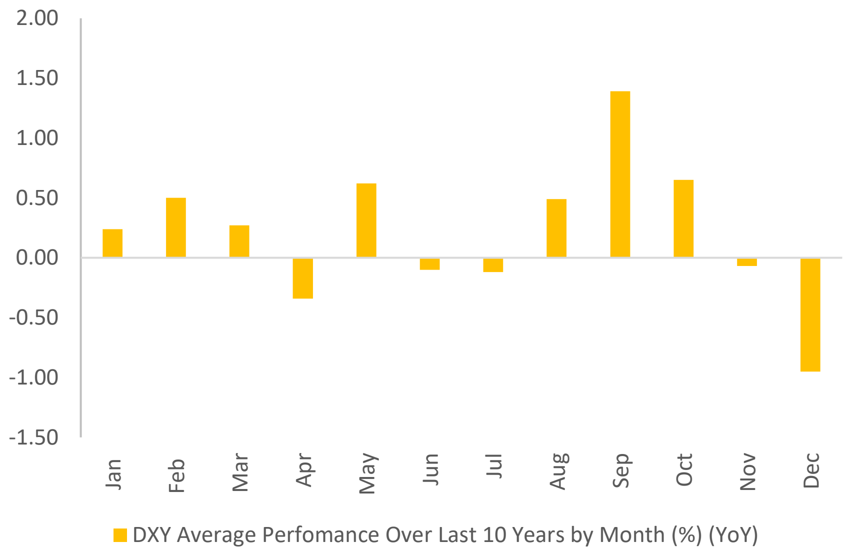
Source: Bloomberg, Maybank FX Research & Strategy
Note: Numbers represent the 24-month rolling correlation between an equal weighted index of USDKRW, USDMYR, USDPHP, USDTHB, USDIDR and USDSGD with the USDJPY, DXY and USDCNY

Developments in the Coming Months Can Guide USD - Asia Pairs Slightly Higher and Asia Central Bank Interventions Intensify

Although we have highlighted that a number of negative factors weighing on the EM Asia FX can dissipate, we still expect that USD – Asia pairs can still head higher in the coming months. The increase in these pairs though can be tempered by the actions of authorities and the limitations of these developments (which we would be elaborating in this section).

There are few factors supporting our belief that USD – Asia pairs can still see some further stress in the coming quarter. The first of those factors we would like to note is the seasonality associated with the DXY. Although the greenback over the last decade can see weakness in Jul, it has tended to be strong in Aug and Sep. This could be due to risk environment during that period tends to be quite subdued in the summer months as the equity markets see weakness and UST yields rise. Given such conditions, the USD-Asia pairs are likely to move higher into the 3Q 2024.

Chart 12: The DXY has Tended to Exhibit More Strength in the Third Quarter



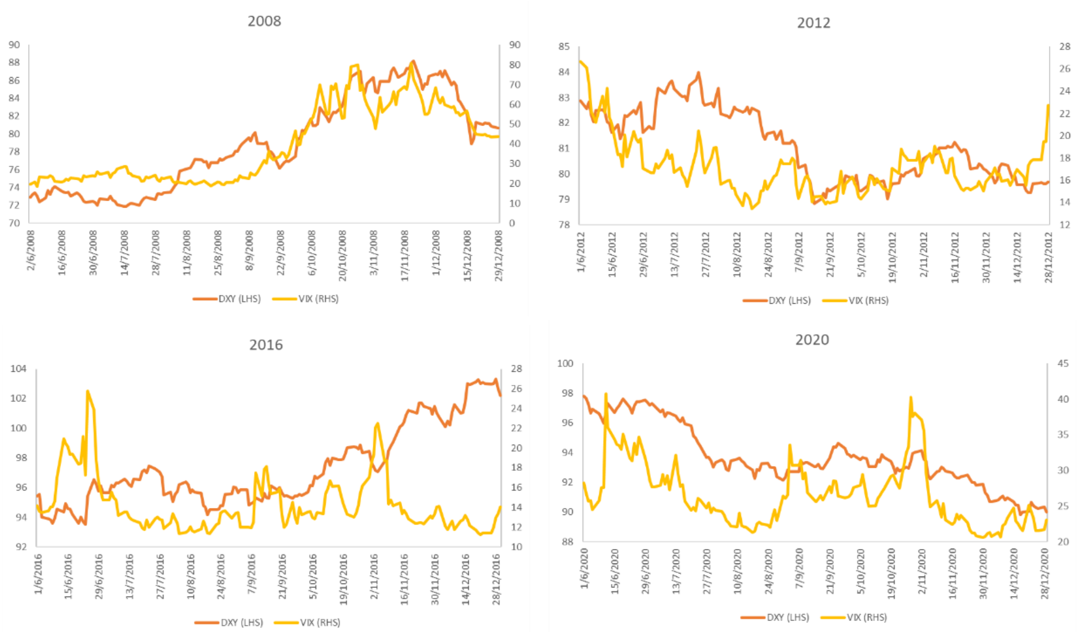
Source: Bloomberg, Maybank FX Research & Strategy

That aside though, we would also like to note that we see it increasingly unlikely that the Fed would soften its tone in the coming months even if a rate cut is on the table in Sep. The Fed is unlikely to want to see an excessive loosening of financial conditions when they do start the easing cycle. As a result, whilst Fed official speak can soften somewhat going into Sep, they are also likely to go at lengths to try to play down any excessive speculation of an aggressive easing cycle. In some sense, a Sep cut could be a hawkish cut. Under such a condition, the USD – Asia may continue to trade elevated. However, we also note that a cut still represents a cut at the end of the day and therefore the upside can be limited.

Building into the next couple of months, the US election campaign is likely to also heat up. However, at this point, following the first Presidential debate and the opinion polls as it stands, it appears that a Trump victory could occur creating concerns of an inflationary environment amid his policies of lower taxes. At this point, we do not see that markets have actually priced in much of the anxiety from the US elections. The reasons why we think so is because market volatility at this point is rather low as we see with the VIX being more subdued. In the past four election cycles (2020, 2016, 2012 and 2008), we tended to see a build-up in volatility after Aug until the election itself in Nov. We note that the DXY performance has been mixed in the past few election cycles. In the 2020 and 2012 election, the DXY actually rose from Aug onwards although it receded after the election in Nov. In the 2016 election, the greenback rose after Aug too and after a brief retracement following the results in Nov, it continued to climb higher, peaking in early Jan. As for 2008, it actually started to rise from Jul onwards and peaked closer towards end Nov, even after the results. We would like to note that the VIX was much higher in 2016 and 2008 when there had been much larger increases in the DXY and the rise in the index had been extended.

In this upcoming election, even as Trump is expected to win, we do note his policies create much anxiety in markets. His talk of pursuing a stronger round of tariffs on various countries can very much risk weighing on the market sentiment and this in turn can guide DXY strength upwards. Also, the Presidential candidate’s push to pursue tax cuts together with the tariffs is actually more supportive of an inflationary environment and accentuate the risk of a higher for longer rates environment. Even so, we do note the passage of such policies are not exactly a certainty depending on how the congressional results pan out to be and the extent that Trump is really going to pursue such high level of tariffs. The Fed would be balancing a difficult game of dealing with the risk of higher prices again and an economy that is likely to see more softening. However, our house view still expects the Fed undertaking two cuts of 25bps each this year from Sep onwards and we believe that should still guide the DXY lower towards end of the year even if heads higher building to and just after the elections.

Chart 13: Both VIX and DXY Only Tend to Climb From Aug Onwards During Years of Presidential Elections Although They Start to Decline After the Nov Results



Source: Bloomberg, Maybank FX Research & Strategy

Another key factor we would also like to note that could still place upward pressure on the USD-Asia pairs in the coming months is the risk of EM central banks cutting ahead of the Fed and giving the DXY support. We do note that the macro situation in Europe is looking less favorable and that cuts ahead of a Fed that may stay hawkish are not ruled out. We also stay cognizant of any further SNB or BOC cuts that could occur ahead of the Fed too. The greenback can get a lift from these cuts in the coming months. For that matter, within the EM Asia space, the BSP is leaning more dovish and this does pose the risk to the PHP. Other regional central banks though are less likely to cut.

Why we Believe that the Upside would also be Limited and that it Can Still Come Back Downwards?

Although we believe that the USD – Asia pairs could head higher into 3Q, we do see that a number of factors going forward could limit the upside. Among those factors include actions taken by EM Asia central banks to support their currencies. As it stands, FX reserves still looks sufficient for quite a number of the countries. If we base it on what would conventionally be seen as criteria for the sufficient level of reserves (three months or more), all the major Asia economies at this point still look to be meeting it.

The option of the central banks to be able to engage in intervention should go some way to at least limit weakness in the currencies. Also, certain central banks have other options to support the currency which include Bank Indonesia (BI) that can issue the SRBI at attractive rates. Malaysian authorities meanwhile have also chosen to coordinate their GLCs/GLICs to convert their foreign currency holdings into local currency to support the MYR. In prior months, we would like to note that a number of EM Asia central banks appear to have intervenedg quite substantially in the market.

Based on our assessment (see Table 4), most of them have been quite aggressive in stabilizing their currency although we find that BI has been more so than the rest. However, we are also wary that currency support measures and interventions can either just provide temporary support to a currency or on the margin prevent some further weakness. We do not see that it can completely stop the weakness and we would like to reiterate that the actions of central banks is only a factor that can go some way to limit the extent of weakness of Asia FX into the next year.

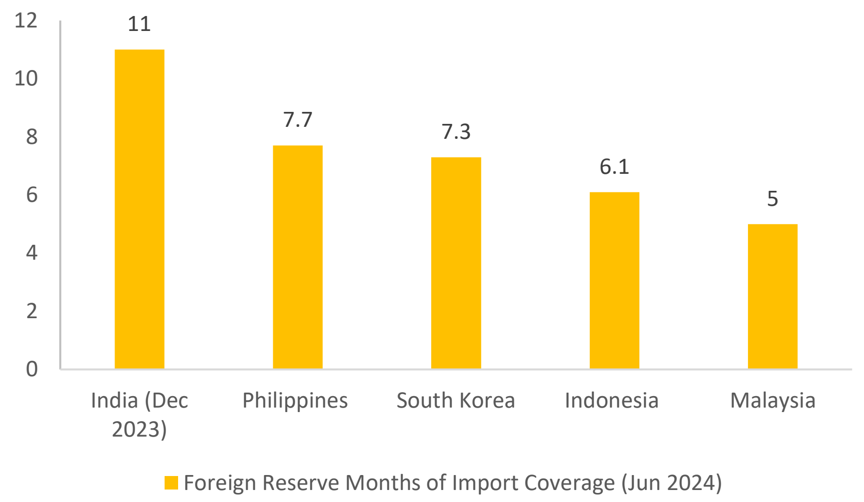
We would though also like to note that other factors which could also limit weakness for Asia FX would be that we are now still looking at an easing from the Fed and not a tightening. Whilst concerns about higher for longer could linger, the Fed would still at the end of the day be on a direction of easing so that would still place a limit on the DXY strength and the upside for USD – Asia pairs.

In the medium – long term, we continue to stick to our trajectory for USD – Asia pairs trending downwards. We hold the view that rates are going to edge down over time as the Fed is likely to gradually ease with softening US data and that should support the USD – Asia pairs moving lower. As it is, there is already a range of US data that are beginning to show quite some declines.

We also would like to mention that greenback strength in the past presidential elections does start to gradually dissipate after the results are out. Even in the case of the 2016 election, whilst the Greenback did climb further just after the results, it began to edge down just a few months after, which shows that the event risk of the presidential election does wear off. After that, greenback strength would depend upon whether subsequent developments are still supportive of it.

However, we would like to note that our view still sees that yields are only expected to come down on a gradual basis and that it is not expected to return to the low rate environment of the pre-pandemic. The Fed is likely to only take a slow approach to easing rates given that the cooling off in the economy is likely to also only be gradual. The Fed moves alone is not the only factor that would limit the extent and pace of the downward moves in yield. It is important to note that the US fiscal situation is quite different from what it has been in the past. The higher expenditure needs could mean that supply can risk offsetting any improvement in demand for treasuries. Meanwhile, treasuries does face competition from other safe haven alternatives that include gold, Chinese GBs, Bitcoin and the CHF. Therefore, USD – Asia pairs are going to come off gradually albeit still trade at elevated levels.

Chart 14: Foreign Reserves of Regional Central Banks is Well Above the International Reserve Adequacy Standard of Three Months



Source: Individual Central Bank Websites, Maybank FX Research & Strategy

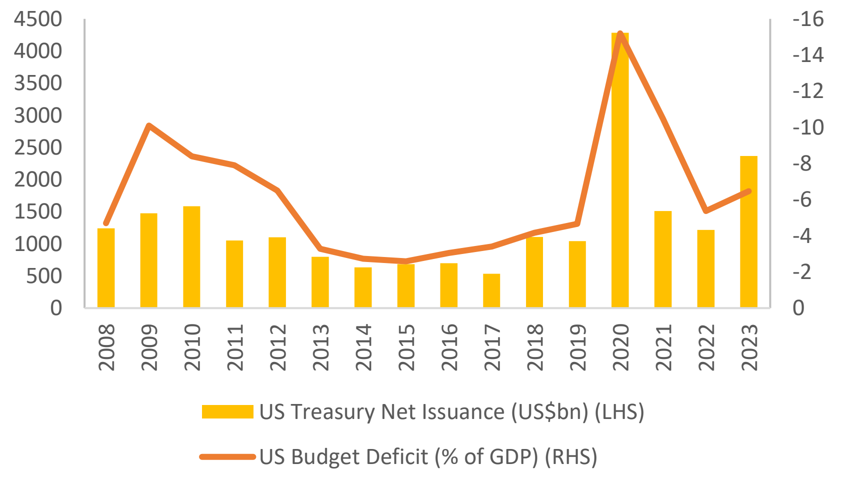
Table 4: EM Asia Central Bank Support Measures

Central Bank	Currency Support Measures*	Policy Rate (Total Increase Since 2021)	Intensity of Currency Support (1 - 5 with 1 being lowest intensity and 5 being the highest)
Bank Indonesia/Government of Indonesia	1. Utilization of Reserves 2. Issuance of SRBI at attractive rates 3. Intervention via the DNDF 4. Natural Resource Firms with Earnings Above $250k Required to Keep 30% of Earnings Onshore for at Least Three Months (BI Offered USD Special Term Deposits) 5. Operation Twist (selling short term notes and buying longer term)	6.25% (+275bps)	4
Bank of Thailand	1. Utilization of Reserves	2.50% (+200bps)	2

Bank Negara Malaysia (BNM)/Government of Malaysia	1. Utilization of Reserves and Forwards 2. Coordinated Conversions of Foreign Currency to Local Currency by GLC/GLICs	3.00% (+125bps)	3
Bank of Korea (BoK)	1. Utilization of Reserves	3.50% (+300bps)	3
Bangko Sentral ng Pilipinas (BSP)	1. Utilization of Reserves	6.50% (+450bps)	3
Reserve Bank of India (RBI)	1. Utilization of Reserves, Forwards and NDFs	4.50% (+150bps)	3
State Bank of Vietnam (SBV)	1. Utilization of Reserves and Forwards (to Keep Currency Within a Band) 2. Issuance of Bills to Reduce Liquidity and Raise Interbank Rates	Refinancing Rate - 4.50% (2021: -, 2022: 200bps 2023: -150bps, Since 2021: Net +50bps)	3
Central Bank of the Republic of China (Taiwan)	1. Utilization of Reserves	2.00% (+87.5bps)	2

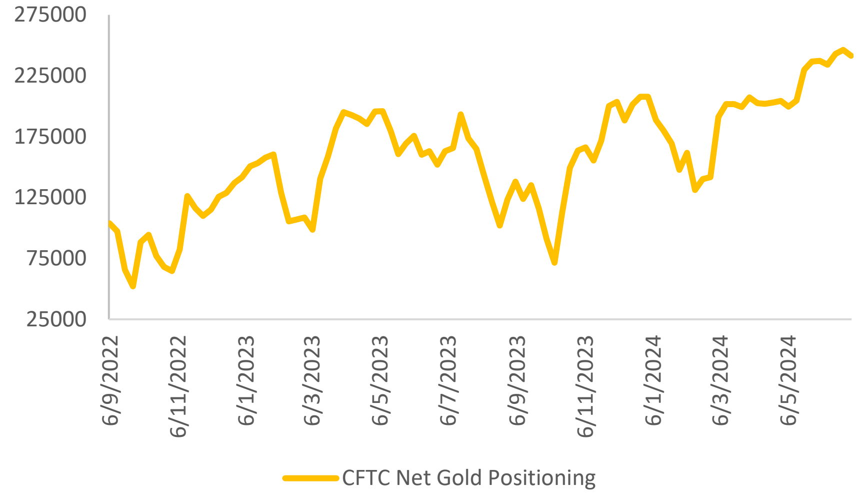
Source: Various news website, Individual Central Bank Websites, Maybank FX Research & Strategy
**Note: The list mainly includes either measures heavily utilized since 2021 or new measures introduced since then. It does not necessarily includes all measures that the country already has in place.*

Chart 15: US Issuance Have Been Rising in Line with the Deficit, Which has Supported Higher Yields



Source: MacroBond, Maybank FX Research & Strategy

Chart 16: Long Positions into Other Safe Havens such as Gold are High



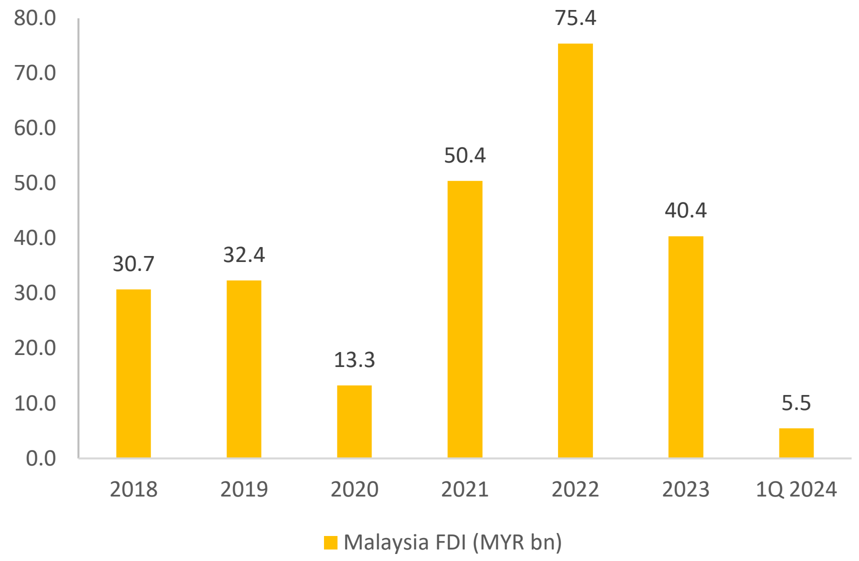
Source: Bloomberg, Maybank FX Research & Strategy

Idiosyncratically, there Could be Some Stronger FDI Flows into a Number of Emerging Markets in Asia

We note that there has been increasing foreign investment interest into certain countries in the regions such as Malaysia. For example, there has been more investor interest into data centers in Malaysia where Google would reportedly be committing $2bn into developing its first data center and cloud region. We also note the possibility of more investments into green tech into Malaysia by foreign players. With the ongoing trade dispute between the US and China, we do not rule out possibility that there could be some further relocation of supply chains towards countries in South East Asia. However, we would like to note that such flows tend to be slower moving and the impact on the currencies could be more spread out over multiple years.

Other factors such as commodity prices are less likely to be a support for currencies such as the IDR in the coming months. Palm oil prices are likely to be more range bound for possibly the next 6 – 9 months given that La Nina is getting pushed further in 2025. We are also cautious about the possibility that a Trump election victory can lead less appetite by the US for renewable diesel. Meanwhile, on oil, prices can still possibly average around $80 - $85 for both Brent and WTI given the balance of geopolitical risks, softer global economy and other supply driven factors. This should prevent too much stress on the external position of many oil importing EM Asia countries such as Thailand, Philippines, Indonesia, Vietnam, South Korea and Taiwan. As for the MYR, the relationship between oil and the currency has broken down over the last few years. For countries such as Indonesia and the Philippines, which have lithium reserves, the commodity still constitutes a much smaller part of its exports. As for coal and Indonesia, the benchmark price may continue to trade around $120 - $140 as Chinese purchasing is likely to be more measured even as energy demand holds up.

Chart 17: FDI Flows Into Malaysia is Above Pre-Pandemic Levels and We Believe it is Likely to Rise in the Future Given Recent Stronger Investor Interest



Source: Bloomberg, Maybank FX Research & Strategy

Taking Note of the Trump Election Victory Risk on EM Asia FX

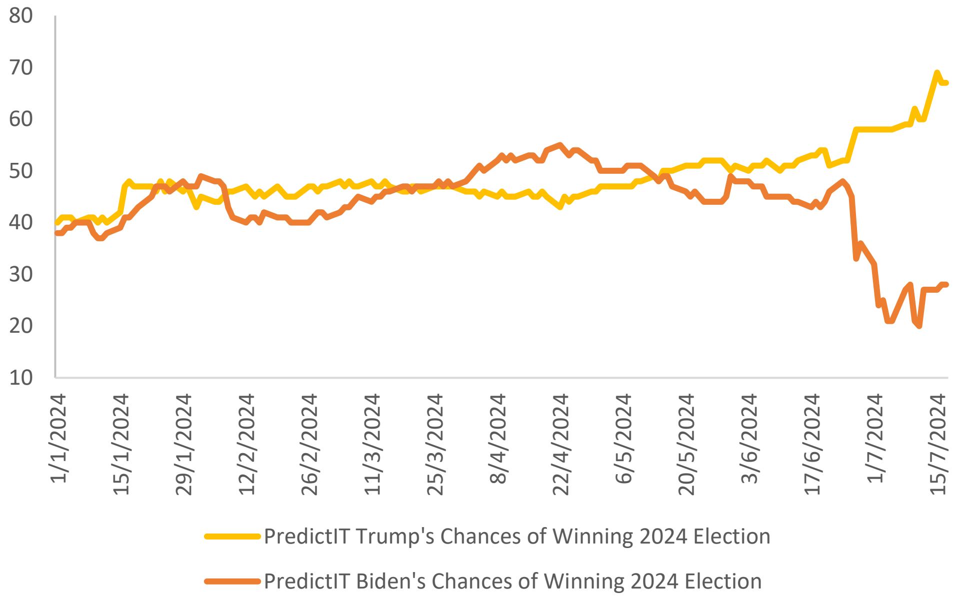
We are cognizant at this point of the higher probability of the risk of a Trump victory playing out, especially with PredictIt now seeing an increased chance that the former President may win in Nov. Policies that the former President is proposing can have wide ranging effects on the global economy. In particular, his advocating of 60% tariffs on all Chinese exports to the US and 10% for all products imported into the US from the rest of the world in addition to tax cuts can have quite substantial impacts on inflation and growth. Rates paths between the US and the rest of the world can risk deviating more strongly in this scenario, which can weigh quite substantially on EM FX including Asia FX.

The possibility that Trump's tariff policies can support an inflationary environment in the US may keep rates higher for longer there and yields elevated. At the same time, the tariffs on Europe (which is more trade focused) can actually weigh on European growth whilst inflation impacts on the continent maybe more subdued as there can be a higher supply of goods from the rest of the world (particularly China) if they do not head to the US. This actually creates conditions for rate cuts in Europe. The Euro trading weaker in this scenario together with the higher US rates can keep the broad USD DXY supported, which may concomitantly also result in sentiment and flows elevating USD – Asia FX.

However, this would only represent one source of negative impact on EM Asia FX from the Trump policies. A trade war spat between the US and China and the tariffs on China can also weigh on EM Asia FX given the risk of further CNY weakness. We had earlier discussed about how EM Asia FX can be quite sensitive to the CNY. We also take note of the possibility that the PBOC may try to limit CNY weakness in such a scenario. Given China's continued export orientation, we are also aware that China and regional growth can be hit by the Trump policies. At the same time, we cannot rule out the possibility of the US also looking to tariff goods on third parties whom China may export their goods through to the US (e.g. China may export its good through another country to the US and the US in turn may choose to tariff that country as such).

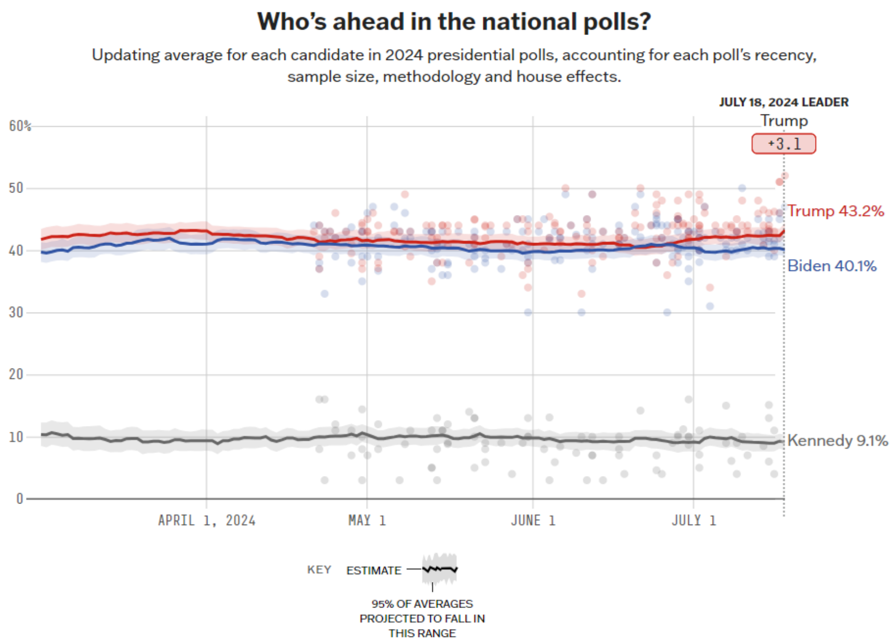
Aside the impact from a rates perspective, we also quite importantly note that flows into EM Asia equity markets can be negatively affected in this environment. The possibility of weaker growth and soft local currencies can further make EM Asia equity markets less attractive and divert more flows possibly to the US equity markets.

Chart 18: PredictIt Seeing Increased Chance of a Trump Victory



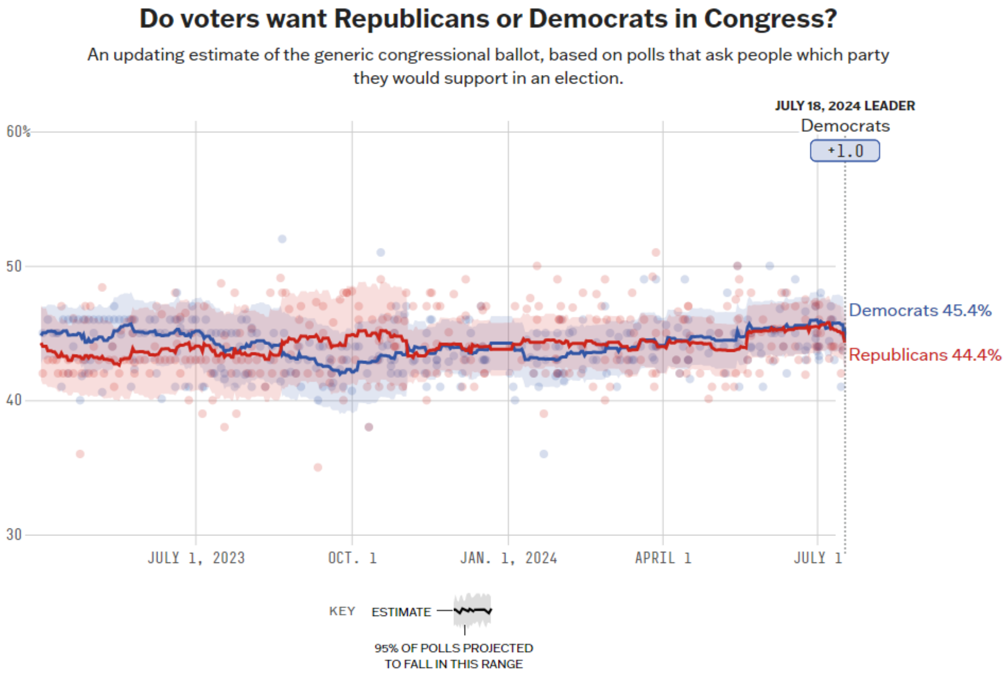
Source: Bloomberg, Maybank FX Research & Strategy

Chart 19: Average of Opinion Polls Shows that Trump has the Lead in the Presidential Race



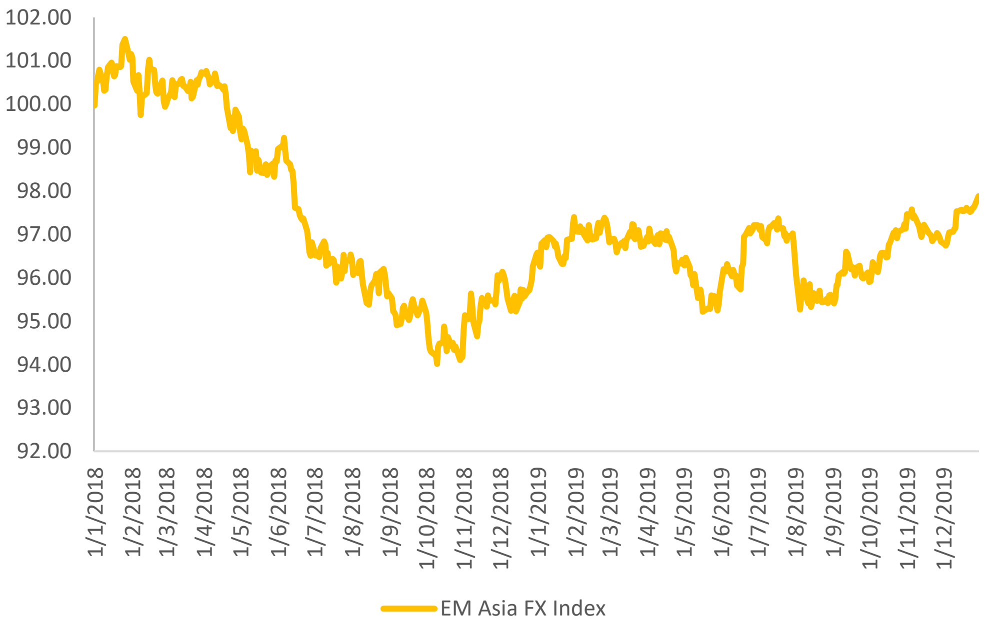
Source: FiveThirtyEight, Maybank FX Research & Strategy
Note: Numbers as of 18 Jul 2024

Chart 20: Average of Opinion Polling Shows that the Race for Congress Remains Extremely Close Between the Republicans and Democrats



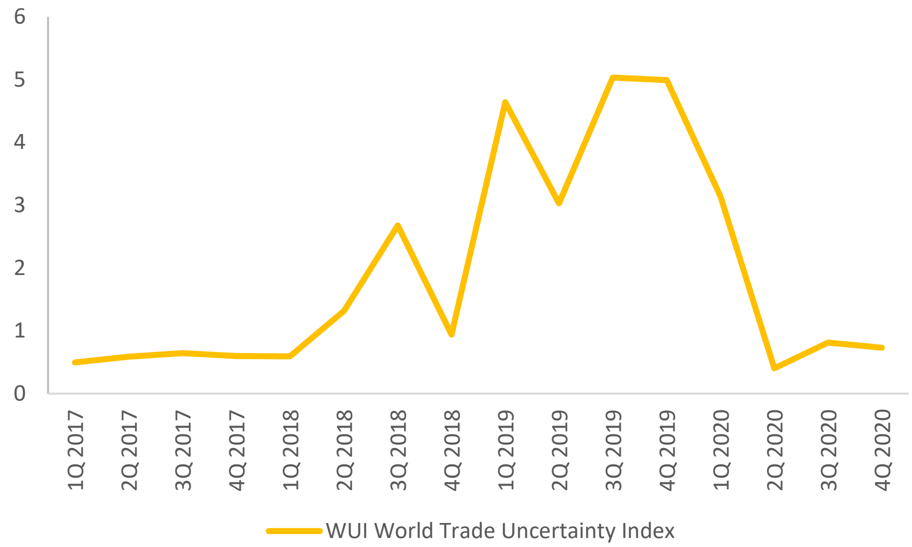
Source: FiveThirtyEight, Maybank FX Research & Strategy
Note: Numbers as of 18 Jul 2024

Chart 21: EM Asia FX took a Dive Initially in 2018 Amid the US - China Trade and Rising Rates Before Stabilizing in 2019 as the Fed Eased Rates Although it Never Fully Recovered Given the Ongoing Trade Spat



Source: Bloomberg, Maybank FX Research & Strategy
Note: EM Asia FX Index is an equal weighted index of MYRUSD, SGDUSD, THBUSD, PHPUSD, IDRUSD, VNDUSD, INRUSD, KRWUSD and TWDUSD and also indexed to a start date of 29/12/2017.

Chart 22: Trade Uncertainty Kept Rising throughout 2018 - 2019 amid the Ongoing Trade War



Source: Bloomberg, Maybank FX Research & Strategy
Note: 1. Higher number denotes greater uncertainty, 2. WUI World Trade Uncertainty Index is compiled and developed by Hites Ahir (International Monetary Fund), Nicholas Bloom (Stanford University) and Davide Furceri (International Monetary Fund).It measures uncertainty related to trade for 143 individual countries on a quarterly basis from 1996 onwards, using the Economist Intelligence Unit (EIU) country reports. The approach to construct the WTU index is to count the number of times uncertainty is mentioned within a proximity to a word related to trade in the EIU country reports. (For more information, please refer to: https://www.policyuncertainty.com/wui_quarterly.html)

Conclusion: There is Still Further Upside for USD - Asia Pairs But We Believe that it would End the Year Lower

Overall, we stick to our forecasts and believe that a peak in USD – Asia pairs can likely come building up to the US Presidential elections and uncertainty on the pace of a Fed cut (whilst other DM and EM central banks could embark on more easing ahead of it). Eventually, the downward trajectory we see is still intact with the presidential election event risk potentially wearing off and the Fed likely to more clearly embark on an easing cycle into next year (unless the Fed does not signal the expected cuts in 2024 from Sep and show reluctance to cut rates). In the near term, as markets continue to price in a Trump re-election effect into the FX markets, the balance of risks is tilted to the upside in the near term for the dollar and negative for EM FX. And with China being the largest source of the U.S. trade deficit, it will be most vulnerable to any punitive trade measures, including other countries that could be targeted such as EM countries such as Mexico, Brazil, South Korea, Taiwan and Vietnam. Recent developments as well [as] the DXY's overvaluation suggest rising risk of a faster move than our forecasts currently imply." The greenback could still hold, though, "especially if the Fed does not immediately endorse market pricing of two - three rate cuts for 2024." The dollar strength has been linked to the Fed's reluctance to cut rates.

Nonetheless, tariff risks aside, our baseline for now is that of a path downward for USD – Asia pairs is one that would be gradual as the Fed itself is also likely to slowly ease whilst other idiosyncratic factors can weigh in on the Asia FX (such as political and fiscal concerns) in addition to geopolitical tensions such as the trade war. In addition, DXY's overvaluation now does suggest there is some risk of a faster move lower relative to what is already priced in now by the markets. We are cognizant of the possibility of more FDI inflows although the flow could be slower in nature and the impact can be more spread out over multiple years, resulting in the effect tending to be something that happens overtime rather than in the next year. Commodities - palm oil are also less likely to be a support for the related EM currencies such as IDR given that China's recovery could still be gradual.

Table 5: Forecasts of Key Regional EM FX

Forecast	3Q 2024	4Q 2024	1Q 2025	2Q 2025
USDIDR	16600	16000	15800	15700
USDPHP	60.00	58.50	58.00	57.00
USDTHB	37.00	35.50	35.00	34.50
USDMYR	4.6500	4.6000	4.5500	4.5000
USDSGD	1.3450	1.3350	1.3300	1.3300
USDKRW	1360	1340	1320	1310
USDVND	25150	25000	25000	24800
USDINR	82.50	82.00	81.00	81.00

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Published by:

Malayan Banking Berhad
(Incorporated in Malaysia)

Saktiandi Supaat
Head, FX Research
saktiandi@maybank.com
(+65) 63201379

Fiona Lim
Senior FX Strategist
fionalim@maybank.com
(+65) 63201374

Alan Lau
FX Strategist
alanlau@maybank.com
(+65) 6320 1378

Shaun Lim
FX Strategist
shaunlim@maybank.com
(+65) 6320 1371